

**38 CFR Part 36****RIN 2900-AR42****Loan Guaranty: Servicer Tier Ranking Procedures**

**AGENCY:** Department of Veterans Affairs.

**ACTION:** Advance notice of proposed rulemaking.

**SUMMARY:** The Department of Veterans Affairs (VA) Loan Guaranty Service (LGY) intends to revise and finalize its temporary regulations governing the assignment of a performance-based tier ranking to each of the servicers that participate in VA's guaranteed home loan program. VA is issuing this advance notice of proposed rulemaking (ANPR) to solicit comments, questions, and information to assist VA in developing a future proposed regulation. Although VA identifies, below, specific topics and questions for discussion, it encourages commenters to discuss any other topic that will help VA develop regulations to assign performance-based tier rankings to servicers that participate in VA's guaranteed home loan program.

**DATES:** Comments must be received on or before **[INSERT DATE 60 DAYS AFTER DATE OF PUBLICATION IN THE FEDERAL REGISTER]**.

**ADDRESSES:** Comments may be submitted through [www.Regulations.gov](https://www.Regulations.gov). Comments received will be available at [www.Regulations.gov](https://www.Regulations.gov) for public viewing, inspection, or copies.

**FOR FURTHER INFORMATION CONTACT:** Andrew Trevayne, Assistant Director for Loan Administration, Loan Guaranty Service (26), Veterans Benefits Administration, Department of Veterans Affairs, 810 Vermont Avenue, NW., Washington, DC 20420, (202) 632-8862. (This is not a toll-free telephone number.)

## **SUPPLEMENTARY INFORMATION:**

### **I. Background**

On February 1, 2008, VA published a final rule, Loan Guaranty: Loan Servicing and Claims Procedures Modifications (VALERI final rule). 73 FR 6293-6368. The VALERI final rule was the result of a lengthy business reengineering process that led to the modernization of VA's loan servicing policies and began a phased implementation of a servicer reporting application called the VA Loan Electronic Interface (VALERI). In the VALERI final rule, VA established temporary procedures for servicer tier ranking, currently codified at 38 CFR 36.4318. 73 FR 6293, 6327; 75 FR 33704-33705.

Section 36.4318(a) states that VA will assign to each servicer a tier ranking based upon the servicer's performance in servicing guaranteed loans. Section 36.4318(a) provides for four tiers, known as tier one, tier two, tier three, and tier four. In the VALERI final rule, VA explained that VA would presume each servicer to rank in tier two until VA develops and implements, via a regulation, a final Tier Ranking System (TRS). 73 FR 6293, 6301. After implementing a TRS, VA would quarterly evaluate each servicer's performance, and annually rank each servicer in tier one, two, three, or four – tier one being the highest rated and tier four the lowest. 38 CFR 36.4318. The VALERI final rule also established servicer loss mitigation options and incentives, currently found at 38 CFR 36.4319 (initially codified at § 36.4819). 73 FR 6293, 6327; 75 FR 33704-33705. Section 36.4319 provides a schedule of incentive payments that VA will pay a servicer in tiers one, two, or three following successful completion of each applicable loss mitigation action or alternative to foreclosure. 38 CFR 36.4319. For the same type of loss mitigation action or alternative to foreclosure, VA will pay servicers in tier one, the highest incentive payment, which will decrease for

tier two, and further decrease for tier three. *Id.* A servicer in tier four will not receive any incentive payment. *Id.*

As noted in the VALERI final rule (and its accompanying proposed rule), VA intended to fully operationalize VALERI, and collect specific, servicer-reported loan servicing and claims data to develop its TRS. 73 FR 6293, 6301. However, due to competing priorities and VALERI reporting limitations, VA has delayed the development and implementation of a TRS. In the meantime, VA continues to presume each servicer to rank in tier two and pays them incentive payments accordingly. See 38 CFR 36.4318, 36.4319. Considering a recent re-design of the VALERI application, which includes enhanced reporting functionality, VA is ready to develop and implement its TRS. By implementing a TRS, VA intends to further encourage its servicers to provide the best level of default resolution and foreclosure avoidance efforts to its borrowers.

## II. Questions for Comment

Once VA's TRS is effective, VA would use the TRS to calculate a quarterly performance score (quarterly score) for each servicer based on servicing data from the prior quarter. 38 CFR 36.4318(c)(1). VA would notify each servicer of its quarterly score. *Id.* After four quarters, VA would aggregate the quarterly scores to derive the annual performance score (annual score) for each servicer. 38 CFR 36.4318(c)(2). Based on the servicer's annual score, VA would assign each servicer a performance tier rank (tier rank) one, two, three, or four. 38 CFR 36.4318(a). Finally, this tier rank would determine the amount of incentive payment that each servicer would receive for each applicable loss mitigation or alternative to foreclosure action that the servicer would complete in the following year. 38 CFR 36.4319. The purpose of this performance-based scoring and tier ranking, and tier-rank-based incentive payments, is to recognize and reward

servicers based on their level of efforts to help borrowers resolve default and avoid foreclosure. Further, it would help identify servicers who may need additional training or assistance in improving their loss mitigation and foreclosure avoidance efforts. Timely default resolution helps borrowers retain their homes, and foreclosure avoidance helps them mitigate the negative impact on their chances of future homeownership.

VA's objective is to develop a TRS that accurately and effectively assesses the performance of each servicer's loss mitigation and foreclosure avoidance efforts. Consequently, the tier-based incentive payments would encourage servicers to timely perform loss mitigation actions that are in the best interest of participants in VA's guaranteed home loan program. With this objective, VA invites comments on the specific questions set forth in this ANPR, and on any other issues that commenters think should be addressed as part of the rulemaking that would establish VA's TRS.

*Question 1: Are there concerns VA should be made aware of that could hinder the implementation of the TRS?*

VA would like to know whether ongoing financial effects of the COVID-19 National Emergency should affect the timing of a TRS implementation. Are there other possible considerations, burdens, or obstacles VA should be made aware of in the implementation of the TRS?

*Question 2: Should VA consider a servicer's volume of VA loans in developing the TRS?*

For servicers who service a small number of VA loans, the performance of one or few seriously delinquent loan(s) would most likely have a volatile effect, good or bad, on the servicer's quarterly/annual score and/or the tier ranking. Should VA consider establishing separate requirements for scoring and ranking

servicers who service a small number of VA loans? If yes, what volume of loans would be an appropriate definition of “small” and why? What information is relevant to understand whether VA should establish separate requirements for this type of servicer? Alternatively, is there another way VA could/should differentiate smaller servicers (i.e., number of annual foreclosure claims)?

*Question 3: Should VA expand the scope of the TRS to include consideration of factors beyond a servicer’s performance in the areas of default resolution and foreclosure avoidance?*

As described above, VA would use the TRS to evaluate and score a servicer’s performance during default resolution and foreclosure avoidance. Further, the tier ranking assigned would be used to determine the amount of incentive paid to the servicer for completing a loss mitigation activity or alternative to foreclosure. With that in mind, should VA limit its entire process of scoring, ranking, and calculating incentive payments to monthly servicer-reported data related to default resolution and foreclosure avoidance, or should VA consider additional factors in its TRS that are not necessarily shown in default resolution and foreclosure avoidance rates? Such factors might include, for example, timely, accurate, and complete reporting of monthly servicer-reported data. Please elaborate on which factors should/should not be included and describe how VA would confirm the successful completion of such factors.

*Question 4: During the testing phase of the TRS, would servicers like to know their quarterly performance scores? If yes, for how many quarters prior to the TRS becoming effective?*

Once the TRS is effective, VA would evaluate an existing servicer’s performance for at least four full quarters to assign the servicer an annual tier ranking. Until then, based on current § 36.4318, VA will continue to presume

each servicer to rank in tier two. VA is not planning to implement a TRS pilot. However, leading up to the TRS becoming effective, VA intends to test certain aspects of the TRS internally with live servicer-reported data. To the extent that VA is able, would there be any benefits to servicers if VA were to provide this information to servicers on a quarterly basis?

*Question 5: What would be the anticipated burden for a servicer to participate in an error resolution process? Should VA provide servicers with such option in developing the TRS?*

To derive the quarterly performance scores for each servicer, the TRS would apply a range of calculations onto a considerable volume of data. VA is considering a number of different criteria upon which to base the quarterly score on servicer performance, including: delinquency rate, roll rate, default resolution rate percentage, quality of service, foreclosure timeline management, data quality and regulatory infractions, and recidivism rate. Subsequently, for each servicer, the TRS would aggregate the quarterly scores to calculate the annual score, and finally, the TRS would use the annual score to assign a tier ranking. It is conceivable that, due to inaccurate or incomplete data, the quarterly score, the annual score, and/or the annual tier ranking could be incorrect.

VA might, within a certain number of days, allow a servicer to contest a quarterly or annual score or annual tier ranking by submitting supporting evidence to VA. VA is interested in understanding the potential burden to servicers to prepare such supporting evidence and submit it to VA.

*Question 6: Should VA consider providing a new VA servicer with a provisional tier ranking after 12 months of servicing has elapsed?*

For a new servicer, including a new servicer who acquires a portfolio of existing VA loans, VA is considering whether to presume the new servicer to rank

in tier two until at least 12 months and four full quarters of servicing has elapsed. Once the new servicer completes at least 12 months and four full quarters of servicing, VA could continue to presume the new servicer to rank in tier two until VA next completes its annual scoring and tier ranking of all servicers. In some cases, this could result in VA presuming a new servicer to rank in tier two for up to 23 months. Alternatively, after the new servicer completes at least 12 months and four full quarters of servicing, VA could assign the new servicer a provisional tier rank based on the quarterly scores of four prior full quarters. The provisional tier rank would be in place until VA next completes its annual scoring and tier ranking of all servicers. VA invites comments as to which approach the public finds more reasonable and why.

*Question 7: Are there other servicer tier ranking systems that VA should review and consider, in part or full, for developing its TRS? Please describe.*

*Question 8: Based on other servicer tier ranking system(s) that servicers may have implemented, approximately how long does it take a servicer to review and understand a new servicer tier ranking system?*

*Question 9: Based on other servicer tier ranking system(s) that servicers may have implemented, as an estimate, what costs and burdens do servicers expect to incur for implementing a new servicer tier ranking system? Please describe the type(s) of cost(s) and provide dollar figures, if available.*

*Question 10: Based on other servicer tier ranking system(s) that servicers may have implemented, what impact, if any, would a lower tier ranking (and smaller incentive payments) have on servicer participation in the VA home loan program? Would smaller incentive payments, due to a lower tier ranking, result in any costs for borrowers, either existing or new?*

Signing Authority

Denis McDonough, Secretary of Veterans Affairs, approved this document on April 12, 2022, and authorized the undersigned to sign and submit the document to the Office of the Federal Register for publication electronically as an official document of the Department of Veterans Affairs.

***Luvenia Potts,***

*Regulations Development Coordinator,*

*Office of Regulation Policy & Management,*

*Office of General Counsel,*

*Department of Veterans Affairs.*

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